

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 04-19**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

Whether certain separately stated fees charged by the Taxpayer in connection with the sale of hardcopy records that are mailed and electronic records that are transmitted electronically are subject to the Tennessee sales and use tax and whether machinery used in the process qualifies as industrial machinery exempt from the tax.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the taxpayer. The rulings herein are binding upon the Department, and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time. Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling and a retroactive revocation of the ruling must inure to his detriment.

FACTS

The Taxpayer provides health and medical record processing services to attorneys, insurance companies, governmental entities, patients, physicians, hospitals, and other requesting parties (the "Customer(s)"). The Taxpayer's services are performed by its employees utilizing equipment (i.e. laptop computers, scanners, etc.) provided by the Taxpayer. These services are performed by the Taxpayer's employees from hospitals, physicians' offices, or employees' home offices located in the State of Tennessee.

In practice, when the Taxpayer receives a request from a Customer for a copy of a patient's health and medical records (the "Information"), the Taxpayer will visit the hospital, physician's office or other location where the particular Information is located. The Taxpayer may facilitate the Customer's request by one of the two following methods which are performed at the hospital, physician's office, or other location where the Information is located:

Method One

The Taxpayer's employee utilizes a laptop computer, scanner, or other similar electronic medium to electronically scan and save the requested Information. Upon securing the scanned Information, the employee electronically transmits the Information to the Taxpayer's facility in [STATE, NOT TENNESSEE]. When the Information is received at the [STATE, NOT TENNESSEE], it is processed and, depending on the Customer's election, either an electronic version of the Information is transmitted to the Customer or a hardcopy version of the Information is printed and mailed to the Customer.

Method Two

The Taxpayer's employee physically photocopies the requested Information and mails it to the Customer from the hospital, physician's office, or other location where the Information was copied.

Invoices

Upon providing any of the above services, the Taxpayer invoices the Customer a separately stated charge for the requested service. The various charges that may be invoiced are explained below:

- Basic/Retrieval Fee: A separately stated flat fee charged for locating the records.
- Quickview Delivery Fee: A separately stated fee to electronically access and view the contents of the delivered Information via the Internet.
- Per Page Fee: A separately stated fee for each page of the Information that is either scanned or photocopied.
- Postage Fee: A separately stated fee for the postage associated with mailing a hardcopy of the individual's Information. This fee does not contain a markup for profit.

- Handling Fee: A separately stated charge, distinct from the charge for postage, associated with mailing a hardcopy of the individual's Information.
- E-Disclose Fee: A separately stated fee to track and confirm the status of the Information being delivered.
- Certification Fee: A separately stated fee to certify the Information.
- Notarization Fee: A separately stated fee to notarize the Information.
- Deposition Fee: A separately stated fee to affirm that the Information is suitable to be utilized in a legal deposition.
- Docustore Fee: A separately stated fee to electronically store the Information.

The Taxpayer concedes that it has nexus with Tennessee for sales and use tax purposes since its employees perform services in Tennessee and the Taxpayer provides them with tangible personal property to use in performing such services.

QUESTIONS PRESENTED

1. Are any of the separately stated fees charged by the Taxpayer subject to Tennessee sales and use tax?
2. Do the scanners, laptop computers and similar electronic media utilized by the Taxpayer qualify as industrial machinery exempt from Tennessee sales and use tax?

RULINGS

1. (a) The basic retrieval fee is subject to Tennessee sales and use tax if the Information sold is provided to a Tennessee Customer in hard copy form after being physically copied or printed from an electronic version.

The basic retrieval fee is not subject to Tennessee sales and use tax if the Information sold is electronically transmitted to a Tennessee Customer after it has been electronically scanned and processed.

- (b) The quickview delivery fee is not subject to Tennessee sales and use tax.

- (c) The per page fee is subject to Tennessee sales and use tax if the Information sold is provided to a Tennessee Customer in hard copy form after being physically copied or printed from an electronic version.

The per page fee is not subject to Tennessee sales and use tax if the Information sold is electronically transmitted to a Tennessee Customer after it has been electronically scanned and processed.

(d) The postage fee is not subject to Tennessee sales and use tax¹.

(e) The handling fee is subject to Tennessee sales and use tax if the Information sold is provided to a Tennessee Customer in hard copy form after being physically copied or printed from an electronic version.

The handling fee is not subject to Tennessee sales and use tax if the Information sold is electronically transmitted to a Tennessee Customer after it has been electronically scanned and processed.

(f) The e-disclose fee is not subject to Tennessee sales and use tax.

(g) The certification fee is subject to Tennessee sales and use tax if the Information sold is provided to a Tennessee Customer in hard copy form after being physically copied or printed from an electronic version.

The certification fee is not subject to Tennessee sales and use tax if the Information sold is electronically transmitted to a Tennessee Customer after it has been electronically scanned and processed.

(h) The notarization fee is subject to Tennessee sales and use tax if the Information sold is provided to a Tennessee Customer in hard copy form after being physically copied or printed from an electronic version.

The notarization fee is not subject to Tennessee sales and use tax if the Information sold is electronically transmitted to a Tennessee Customer after it has been electronically scanned and processed.

(i) The deposition fee is subject to Tennessee sales and use tax if the Information sold is provided to a Tennessee Customer in hard copy form after being physically copied or printed from an electronic version.

The deposition fee is not subject to Tennessee sales and use tax if the Information sold is electronically transmitted to a Tennessee Customer after it has been electronically scanned and processed.

(j) The docustore fee is not subject to Tennessee sales and use tax.

2. Yes, provided that the Taxpayer can show that its copy machines, scanners, laptop computers, printers and other machinery used to produce the hard copies of Information

¹ Under Tennessee's streamlined sales and use tax statutes effective July 1, 2005, postage and other delivery charges will be subject to sales and use tax. Tenn. Code Ann. § 67-6-102(48)(A)(iv) will include "delivery charges" in the "sales price" subject to sales and use tax. Tenn. Code Ann. § 67-6-102(13) will define "delivery charges" as ". . . charges by the seller of personal property or services for preparation and delivery to a location designated by the purchaser of personal property or services including, but not limited to, transportation, shipping, postage, handling, crating, and packing[.]"

sold to Customers are used for that purpose for at least 51% of the time that they are in use.

ANALYSIS

Applicable Statutes, Rules, and Case Law

Tenn. Code Ann. § 67-6-202(a) levies the sales tax on “. . . the privilege of engaging in the business of selling tangible personal property at retail . . .” and Tenn. Code Ann. § 67-6-702(a) authorizes Tennessee counties and incorporated cities to levy local sales taxes on the same privileges. “Sale at retail” also includes the furnishing of certain things or services enumerated in Tenn. Code Ann. § 67-6-102(a)(25)(F). Tenn. Code Ann. § 67-6-102(a)(25)(B) and (F).

“Tangible personal property” is defined by Tenn. Code Ann. § 67-6-102(a)(31) to mean and include “. . . personal property, which may be seen, weighed, measured, felt or touched, or is in any other manner perceptible to the senses.”

The transfer of Information into a Customer’s computer manually or by magnetic tape, telephone lines, punch cards or other means for a charge does not constitute the sale of tangible personal property and thus is not subject to Tennessee sales and use tax. *Commerce Union Bank v. Tidwell*, 538 S.W.2d 405 (Tenn. 1976).

Tenn. Code Ann § 67-6-202(a) further provides that the tax is “. . . levied on the **sales price** of each item or article of tangible personal property when sold at retail in this state . . .” (Emphasis added.)

“Sales price” is defined by Tenn. Code Ann. § 67-6-102(a)(28) to mean:

. . . the total amount for which a taxable service or tangible personal property is sold, **including any services that are a part of the sale of tangible personal property** . . . (Emphasis added.)

Charges for services provided in connection with the sale of tangible personal property are subject to Tennessee sales and use tax even though the services, standing alone, would be non-taxable. *Thomas Nelson, Inc. v. Olsen*, 723 S.W.2d 621 (Tenn. 1987).

T.C.A. § 67-6-206(a) creates a sales tax exemption for the purchase of industrial machinery by stating that “. . . no tax is due with respect to industrial machinery.”

“Industrial machinery” is defined by T.C.A. § 67-6-102(a)(14)(C) to include:

Machinery utilized in the pre-press and press operations in the business of printing, including plates and cylinders and including the component parts and fluids or chemicals necessary for the specific mechanical or chemical actions or operations of

such machinery, plates and cylinders, regardless of whether or not the operations occur at the point of retail sales.

The Department of Revenue has promulgated Tenn. Comp. R. & Regs. 1320-5-1-.67 regarding printed matter:

(1) Sales of advertising circulars, books, forms, tickets, and other like printed items of tangible personal property are subject to the sales and use tax unless the printed matter is sold for resale purposes. The sales or use tax is based upon the selling price, without any deductions therefrom, except the value of the postage included on printed envelopes furnished to customers.

(2) The printing and binding of paper, books, forms, letters, and the like is a fabrication thereof, and is subject to the sales or use tax unless the fabrication is a part of a manufacturing process for resale. It is immaterial whether the customer furnishes any or all of the paper or other materials used in the fabrication work. Any rebinding or other repair of a book or other tangible personal property is subject to the sales or use tax.

(3) Any equipment, materials and supplies which are not sold to a customer, or which do not become a component part of the printed matter being fabricated for sale, or which cannot qualify as an industrial supply exempt from tax, are subject to the sales or use tax. In those cases where a printer makes a specific charge in a contract, or indicates a specific charge on an invoice for an engraving, die, plate, or any other similar kind of tangible personal property sold to a customer, and uses the property in the printing process, he shall be liable for the tax represented by such sale or use irrespective of whether the customer ever actually obtains possession of the engraving, die plate, etc., or whether the printed matter itself is subject to the sales or use tax.

In *Rivergate Toyota, Inc. v. Huddleston*, WL 83720 (Tenn. Ct. App. 1988), the court, citing Tenn. Comp. R. & Regs. 1320-5-1-.67(1), held that postage charged to customers for the mailing of printed items is not subject to Tennessee sales and use tax.

Application of Statutes, Rules and Case Law to the Charges Made

First, it is important to note that the Taxpayer's electronic transmission of Information to a Tennessee Customer for consideration after it has been electronically scanned and processed does not constitute the sale of tangible personal property. See *Commerce Union Bank v. Tidwell*, 538 S.W.2d 405 (Tenn. 1976). It is the sale of a service, but it is not one of the taxable services enumerated in Tenn. Code Ann. § 67-6-102(a)(25)(B) and (F). Accordingly, such a transaction is not subject to Tennessee sales and use tax.

However, when electronically scanned and processed Information is printed in hard copy form and mailed to a Tennessee Customer for consideration, a sale of tangible personal property (the hard copy) has occurred and the Tennessee sales and use tax applies. Tenn. Code Ann. § 67-6-202(a) and Tenn. Code Ann. § 67-6-102(a)(31).

Likewise, when Information is physically photocopied and the resulting hard copy is mailed to a Tennessee Customer for consideration, a sale of tangible personal property (the hard copy) has occurred and the Tennessee sales and use tax applies.

Basic Retrieval Fee

The Taxpayer may charge its Customer a separately stated flat fee for locating the records required.

As explained above, when the Information is provided to a Tennessee Customer for consideration in hard copy form after being physically copied or printed from an electronic version, a sale of tangible personal property has occurred. Tenn. Code Ann. § 67-6-202(a) and Tenn. Code Ann. § 67-6-102(a)(31). Since the “sales price” of the item sold is defined by Tenn. Code Ann. § 67-6-102(a)(28) to include any services that are a part of the sale of tangible personal property, the basic retrieval fee is included in the sales price of the tangible personal property sold and therefore is subject to Tennessee sales and use tax. *See Thomas Nelson, Inc. v. Olsen*, 723 S.W.2d 621 (Tenn. 1987).

When the Taxpayer electronically transmits Information to a Tennessee Customer for consideration after it has been electronically scanned and processed, no sale of tangible personal property has occurred. *See Commerce Union Bank v. Tidwell*, 538 S.W.2d 405 (Tenn. 1976). The sale of a service has taken place, but the service sold is not one of the taxable services enumerated in Tenn. Code Ann. § 67-6-102(a)(25)(B) and (F). Accordingly, such a transaction is not subject to Tennessee sales and use tax and the basic retrieval fee is not subject to the tax.

Quickview Delivery Fee

The Taxpayer charges this fee to its Customer for the privilege of electronically accessing and viewing the contents of delivered Information via the Internet.

When a Customer purchases the privilege of electronically accessing and viewing the contents of delivered Information via the Internet, there has been no sale of tangible personal property and the service purchased is not one of the taxable services enumerated in Tenn. Code Ann. § 67-6-102(a)(25)(B) and (F). Therefore, the quickview delivery fee is not subject to Tennessee sales and use tax.

Per Page Fee

This is a fee that the Taxpayer charges its Customer for each page of Information that is scanned or photocopied. The taxability of this fee turns on whether the ultimate primary transaction is a sale of tangible personal property or a taxable service because Tenn. Code Ann. § 67-6-102(a)(28) provides that the total amount for which a taxable service or tangible personal property is sold, includes any services that are a part of the sale.

If the Taxpayer for consideration electronically transmits Information to a Tennessee Customer after it has been electronically scanned and processed, no sale of tangible personal property has occurred. See *Commerce Union Bank v. Tidwell*, 538 S.W.2d 405 (Tenn. 1976). A service has been sold, but it is not one of the taxable services enumerated in Tenn. Code Ann. § 67-6-102(a)(25)(B) and (F). Accordingly, the per page fee charged for scanning each page of Information is not subject to Tennessee sales and use tax.

However, when electronically scanned and processed Information is printed in hard copy form and mailed to a Tennessee Customer for consideration, a sale of tangible personal property (the hard copy) has occurred. Tenn. Code Ann. § 67-6-202(a) and Tenn. Code Ann. § 67-6-102(a)(31). A sale of tangible personal property also occurs when Information is physically photocopied and the resulting hard copy is mailed to a Tennessee Customer for consideration.

In these situations, the per page fee charged for scanning each page of Information is subject to Tennessee sales and use tax because it is part of the sale of tangible personal property (the hard copy) that ultimately results from the process. Tenn. Code Ann. § 67-6-102(a)(28). See *Thomas Nelson, Inc. v. Olsen*, 723 S.W.2d 621 (Tenn. 1987).

Postage Fee

A postage fee that does not contain a profit mark-up is charged for mailing hardcopy Information to the Taxpayer's Customer².

Tenn. Comp. R. & Regs. 1320-5-1-.67(1) states that:

- (1) Sales of advertising circulars, books, forms, tickets, and other like printed items of tangible personal property are subject to the sales and use tax unless the printed matter is sold for resale purposes. The sales or use tax is based upon the selling price, without any deductions therefrom, except the value of the postage included on printed envelopes furnished to customers.

The Taxpayer is selling tangible personal property (hard copy) printed Information to its Tennessee Customers that is subject to Tennessee sales and use tax. The above cited Tenn. Comp. R. & Regs. 1320-5-1-.67(1) states that the value of postage included in the selling price of printed items of tangible personal property is not subject to sales and

² Under Tennessee's streamlined sales and use tax statutes effective July 1, 2005, postage and other delivery charges will be subject to sales and use tax (see footnote 1).

use tax. In *Rivergate Toyota, Inc. v. Huddleston*, WL 83720 (Tenn. Ct. App. 1988), the court, citing Tenn. Comp. R. & Regs. 1320-5-1-.67(1), held that postage charged to customers for the mailing of printed items is not subject to Tennessee sales and use tax.

Accordingly, the postage fee that the Taxpayer charges its Customers for mailing hardcopies of Information, whether printed from an electronic version or physically photocopied, is not subject to Tennessee sales and use tax.

Handling Fee

This is a charge, separate from postage, associated with the mailing of hardcopy Information to Tennessee Customers.

When Information is provided to a Tennessee Customer for consideration in hard copy form after being physically copied or printed from an electronic version, a sale of tangible personal property has occurred. Tenn. Code Ann. § 67-6-202(a) and Tenn. Code Ann. § 67-6-102(a)(31). Since the “sales price” of the item sold is defined by Tenn. Code Ann. § 67-6-102(a)(28) to include any services that are a part of the sale of tangible personal property, the handling fee is included in the sales price of the tangible personal property sold and therefore is subject to Tennessee sales and use tax. See *Thomas Nelson, Inc. v. Olsen*, 723 S.W.2d 621 (Tenn. 1987).

If the Taxpayer electronically transmits Information to a Tennessee Customer for consideration after it has been electronically scanned and processed, no sale of tangible personal property has occurred. See *Commerce Union Bank v. Tidwell*, 538 S.W.2d 405 (Tenn. 1976). The sale of a service has taken place, but the service sold is not one of the taxable services enumerated in Tenn. Code Ann. § 67-6-102(a)(25)(B) and (F). Accordingly, such a transaction is not subject to Tennessee sales and use tax and the handling fee is not subject to the tax.

E-Disclose Fee

This fee is charged by the Taxpayer to track and confirm the status of Information that is being delivered to a Customer.

This fee is for the service of providing the Taxpayer’s customer with information regarding the status of the customer’s order. Regardless of whether the final product being delivered to the Customer is tangible or intangible personal property, information regarding the status of the Customer’s order is in no way a part of the tangible or intangible personal property being sold.

Accordingly, the e-disclosure fee is for a nontaxable service and is not subject to Tennessee sales and use tax.

Certification Fee

This is a fee charged by the Taxpayer to certify Information sold to the Customer.

The taxability of this fee depends on whether a sale of tangible personal property has taken place. In cases where the Information sold to the Tennessee Customer is in hard copy form, a sale of tangible personal property has occurred. Tenn. Code Ann. § 67-6-202(a) and Tenn. Code Ann. § 67-6-102(a)(31). The certification fee is thus taxable because Tenn. Code Ann. § 67-6-102(a)(28) defines “sales price” to include any services that are a part of the sale of tangible personal property. See *Thomas Nelson, Inc. v. Olsen*, 723 S.W.2d 621 (Tenn. 1987).

The certification fee is not subject to Tennessee sales and use tax when the Taxpayer electronically transmits Information to a Tennessee Customer for consideration after it has been electronically scanned and processed because no sale of tangible personal property has occurred. See *Commerce Union Bank v. Tidwell*, 538 S.W.2d 405 (Tenn. 1976). Thus, the transaction is not subject to Tennessee sales and use tax and the certification fee is not subject to the tax.

Notarization Fee

A fee is charged for notarizing Information that the Taxpayer sells to Customers.

If a sale of tangible personal property is involved, as is the case when the Information is provided to a Tennessee Customer for consideration in hard copy form after being physically copied or printed from an electronic version, the notarization fee is taxable because Tenn. Code Ann. § 67-6-102(a)(28) defines “sales price” to include any services that are a part of the sale of tangible personal property. Tenn. Code Ann. § 67-6-202(a) and Tenn. Code Ann. § 67-6-102(a)(31). See *Thomas Nelson, Inc. v. Olsen*, 723 S.W.2d 621 (Tenn. 1987).

The notarization fee is not subject to Tennessee sales and use tax when the Taxpayer electronically transmits Information to a Tennessee Customer for consideration after it has been electronically scanned and processed because no sale of tangible personal property has occurred. See *Commerce Union Bank v. Tidwell*, 538 S.W.2d 405 (Tenn. 1976).

Deposition Fee

A deposition fee is charged when the Taxpayer affirms that the Information sold is suitable to be utilized in a legal deposition.

The deposition fee is subject to Tennessee sales and use tax only when the Information being sold to a Tennessee Customer is in hardcopy form and thus is tangible personal property. Tenn. Code Ann. § 67-6-202(a) and Tenn. Code Ann. § 67-6-102(a)(31). Since the “sales price” of the item sold is defined by Tenn. Code Ann. § 67-6-102(a)(28) to include any services that are a part of the sale of tangible personal property, the

deposition fee is included in the sales price of the tangible personal property sold and therefore is subject to Tennessee sales and use tax. See *Thomas Nelson, Inc. v. Olsen*, 723 S.W.2d 621 (Tenn. 1987).

In situations where the Taxpayer electronically transmits Information to a Tennessee Customer for consideration after it has been electronically scanned and processed, the sale of a nontaxable service, rather than the sale of tangible personal property, has occurred. See *Commerce Union Bank v. Tidwell*, 538 S.W.2d 405 (Tenn. 1976). Therefore, the deposition fee is not subject to the Tennessee sales and use tax in such a situation.

Docustore Fee

This fee is charged for the electronic storage of Information.

A sale of tangible personal property has not occurred when Information sold is electronically transmitted or electronically stored. See *Commerce Union Bank v. Tidwell*, 538 S.W.2d 405 (Tenn. 1976). The sale of services has taken place, but the services sold are not any of the taxable services enumerated in Tenn. Code Ann. § 67-6-102(a)(25)(B) and (F). Accordingly, such a transaction is not subject to Tennessee sales and use tax and the docustore fee is not subject to the tax.

Application of Statutes, Rules and Case Law to Industrial Machinery

“Industrial machinery” is defined by T.C.A. § 67-6-102(a)(14)(C) to include “[m]achinery utilized in the pre-press and press operations in the business of printing . . .” It is important to note that, unlike other industrial machinery statutes, this particular statute does not require the “principal” business to be manufacturing, as determined by the 51% test of *Tennessee Farmers’ Cooperative v. Jackson*, 736 S.W.2d 87 (Tenn. 1987), in order to qualify for the industrial machinery exemption. However, in order for the machinery to qualify, it must be “. . . utilized . . . in the business of printing.”

The Taxpayer uses copy machines to make hard copies of original Information documents that it sells to Tennessee Customers. It also uses laptop computers and printers to print hard copies of Information after it has been electronically scanned and processed. The printed hard copies are then sold to Customers. Thus, the Taxpayer is engaged in the “business of printing.”

However, in order for the copy machines, scanners, laptop computers, printers and other machinery used to produce the hard copies to qualify as industrial machinery exempt from Tennessee sales and use tax, they must be “. . . utilized . . . in the business of printing.” The equipment in question is not being utilized in the business of printing when it is used only to scan and process Information documents and electronically transmit the Information to Customers. Thus, such equipment is utilized only part of the time in the business of printing.

Although tax statutes are generally construed in favor of the taxpayer, exemptions to tax statutes are strictly construed against the taxpayer, who has the burden of proving entitlement to the exemption. *Cape Fear Paging Co. v. Huddleston*, 937 S.W.2d 787, 788 (Tenn. 1996); *Covington Pike Toyota, Inc. v. Cardwell*, 829 S.W.2d 132, 135 (Tenn. 1992).

In situations where machinery is utilized only part of the time in an activity that would qualify it as industrial machinery exempt from Tennessee sales and use tax, this Department has allowed the exemption if the machinery was utilized in the qualifying activity at least 51% of the time that it is in use.

The facts given do not state how much of the time the machinery in question is used in the production of Information sold in hard copy form and how much time it is used in the production of Information sold in electronic form. However, if the Taxpayer can show that its copy machines, scanners, laptop computers, printers and other machinery used to produce the hard copies of Information sold to Customers are used for that purpose for at least 51% of the time that they are in use, then such equipment will qualify as industrial machinery exempt from Tennessee sales and use tax.

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APPROVED: Loren L. Chumley, Commissioner

DATE: 07/29/04